

Helpful Hints to Avoid Penalties



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This guide is designed to assist Tribal entities by providing insights on actions they can undertake to minimize potential penalties. It is not all inclusive, and your local ITG Specialist is available to address any questions that are not adequately covered within this document.

Receiving a Notice From IRS

Tribal governments or other tribal entities occasionally receive notices from the Internal Revenue Service. These notices arise from various situations such as failure to deposit payroll taxes timely, and late filing or non-filing of various returns. The two most important things to do are:

- Determine, through a review of your records, if the notice is correct, AND
- Respond to the notice on or before the date required.

Failure to respond timely can lead to the assessment of penalties and interest. Failure to review records to ensure the correctness of the notice can lead to payment of unnecessary penalties. If the notice is determined to be correct and additional tax, penalties, and interest are due; payment should be made within the time frame shown in the notice.

Indian Tribal Government Specialists and other IRS personnel are ready to assist you in understanding the notices and determining their accuracy. Our Customer Account Services staff can be contacted toll-free at **1-877-829-5500**. This call center is open from 8:00 am to 4:30 pm eastern time.

ITG Specialists are also available to assist when a timely response to an incorrect notice does not achieve a satisfactory resolution to the situation. The ITG Specialist can review your response and help you file the proper forms to resolve the issue or ensure the case is routed to the proper office for resolution.

SSA and IRS Reconciliation Processes

As the Social Security Administration (SSA) processes employer wage reports, it maintains a record of total Social Security and Medicare wages and tips processed for each employer. These totals are then compared with the totals for Internal Revenue Service (IRS) employment tax records filed by the employer with IRS on Form 941 returns. Employers whose reports to IRS and SSA do not balance are contacted for an explanation of the discrepancy and asked for additional wage evidence.

- IRS contacts employers who reported more wages to SSA than to IRS.
- SSA contacts employers who reported more wages to IRS than to SSA.

Failure to resolve these discrepancies may result in IRS assessment of penalties for filing incorrect reports.

When more wages were reported to IRS than to SSA, the SSA is concerned that employees' earnings are not credited correctly to the agency's records. SSA examines some of these cases and makes an effort to resolve the difference without contacting the employer.

When an effort to resolve the discrepancy is unsuccessful or a resolution is not possible without the employer's assistance, SSA sends a notice and questionnaire to the employer, requesting the earnings data needed to resolve the case. If SSA does not receive a response after 120 days, the employer is sent a second notice. When no response is received after the second notice, IRS is responsible for contacting the employer and may impose penalties, if necessary.

Balancing Forms 941 to Form W-3 Information

You should balance or reconcile your Form 941 reports to your Form W-3 for the year. This will help you identify and resolve errors in your records to avoid the filing of erroneous reports. You should balance cumulative quarterly Forms 941 for the tax year to the Form W-2/W-3 information in your records at the end of the tax year.

Compare the amounts you reported to SSA on Form W-3 to the sum of the amounts you reported to IRS on Forms 941 for the tax year.

Review your copies of filed Forms 941 for the year along with the payroll records for the year. Identify any over or under reporting of income or wages, and adjust any overpayment or underpayment of taxes on the Form 941 for the erroneous quarter. For example, a 2007 reporting error discovered during April 2008 would be an adjustment on the second quarter 2008 Form 941. Form 941c is not a stand-alone form; it must be filed with the next quarter's Form 941.

Annual amounts from payroll records should match the total amounts reported on all Forms 941 for the year; the total amounts reported on all Forms 941 for the year should match the sum of the same data fields which are shown in the W-3 totals. If these amounts do not match, recheck records and identify necessary adjustments.

To assist you with this process, a worksheet has been provided on the following page.

Forms 941, W-2, and W-3 Reconciliation

- Annual amounts from payroll records should match the total amounts reported on all Forms 941 for the year.
- Total amounts reported on all Forms 941 for the year should match the sum of the same data fields shown in the W-3 totals.
- If these amounts do not match, recheck records and identify necessary adjustments.

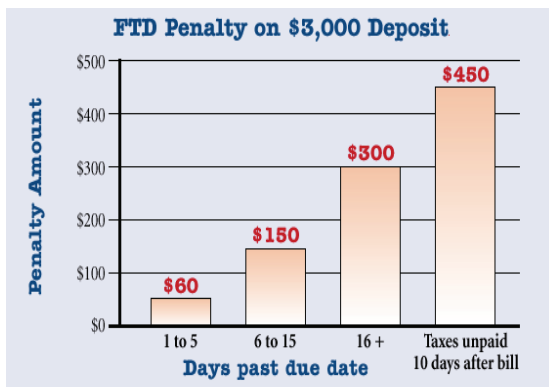
column a	column b	column c	column d	column e	column f	column g
COMPARISON AREA	941 Line #	Form 941 (all 4 quarters)	W-2, W-3 Box #	W-2s (total of all forms)	Amount on W-3	Difference (col c minus col e)
Compensation	Line 2		Box 1			
Federal Income Tax	Line 3		Box 2			
Social Security Wages	Line 5a Col. 1		Box 3			
Social Security Tips	Line 5b Col. 1		Box 7			
Social Security Tax	Line 5a + 5b Col. 2					
Social Security Tax comparison computation	Line 5a + 5b (column 2) divided by 2		Box 4			
Medicare Wages	Line 5c Col. 1		Box 5			
Medicare Tax	Line 5c Col. 2					
Medicare Tax comparison computation	Line 5c (column 2) divided by 2		Box 6			

The Basics of Federal Tax Deposits

When you pay your employees, you do not pay them all of the money they have earned. The income tax and the FICA (Social Security and Medicare) that you withhold from your employees' paycheck are part of their wages. Even though you pay these withheld taxes to the United States Treasury, they are still your employees' earnings.

The portion of your employees' wages that you withhold for transmitting to the Treasury is called "Trust Fund" taxes. Through this withholding, your employees pay their contributions toward their retirement benefits (Social Security and Medicare) and the income taxes reported on their own tax returns. Your employees' trust fund taxes, along with the employer's matching share of FICA, are paid to the Treasury through the Federal Tax Deposit (FTD) System.

You should deposit these amounts on time for the employees' benefit. Postponing the tax deposit isn't the same as using your own money to make late payment on a phone bill or to a supplier. Congress established large penalties for employers that delay in turning over employment taxes to the Treasury. If you delay paying that money, the more it could cost you.



To illustrate how much it will cost you to make your Federal Tax Deposits late, consider this example. Assume your monthly liability for withheld income tax, Social Security and Medicare tax, and your employer's matching share totals \$3,000 per month. Review the graph to see how quickly a penalty for making late deposits increases. As you can see, using your trust fund taxes to finance your other operating expenses can be very costly.

The FTD penalty is computed by multiplying the amount of tax you have underpaid by a penalty percentage rate based on how many days late you make the deposit. These penalties for late deposits are expensive. For amounts not properly or timely deposited, the penalty rates are shown on the table at the right.

Failure to Deposit Penalty Percentage Rates	
Cause for Penalty	Penalty Percentage Rate
Deposits made 1-5 days late	2%
Deposits made 6-15 days late	5%
Deposits made 16 + days late	10%
Taxes unpaid after the 10th day following the 1st IRS bill	15%
Deposit made at unauthorized financial institution	10%
Amounts subject to Electronic Deposit requirements but not deposited via EFTPS	10%

In addition to the deposit penalties, you will also be subject to penalties if you late file your Form 941 or don't pay the amount due on the return as shown on the table at the right.

Please review your payroll procedures to determine if you are making timely deposits. When you make timely deposits, you avoid penalties. When you avoid penalties, money is available for other governmental needs. Don't let penalties get out of hand. They **are** avoidable!!!

Other Penalties		
	RATE	MAXIMUM
Late Filed Tax Return	5% per month of unpaid tax	25%
Late Paid Tax	½% per month of unpaid tax, then 1% after Notice of Intent to Levy	25%

Who must make deposits?

Deposits are **required** if you file Form 941 with \$2,500 or more in taxes per quarter.

What taxes must be deposited?

- Income tax withheld from your employees
- FICA (Social Security and Medicare) tax withheld from your employees
- FICA (Social Security and Medicare) — the employer's share

Important Difference

- Making deposits and filing employer returns with payments are not the same.
- Taxes are **reported** by filing, and **paid** by depositing.

When should you make Form 941 tax deposits?

- If your total taxes for the quarter are less than \$2,500, they can be paid with the return or deposited by the return due date.
- If your total taxes on Form 941 are \$2,500 or more, you'll need to determine which deposit schedule to follow (monthly or semi-weekly).
- The easiest/safest way is to make a deposit the **same day** you make payroll or **no later than the deposit due date**.

For further explanation of when to deposit see Publication 15 page 19 through 21.

Exceptions to Deposit Schedules

\$100,000 Next-Day Deposit Rule:

- If you accumulate a tax liability of **\$100,000 or more on any day** during a deposit period, you must deposit the tax by the **NEXT banking day**, whether you are a monthly or semiweekly schedule depositor.
- Once you meet the \$100,000 next-day rule, you follow the semiweekly schedule for all deposits less than \$100,000. You are a semiweekly schedule depositor for the rest of the year, and during all of the next calendar year.
- Since the bank usually needs **24 hours to make the deposit**, you need to request the deposit the same day that you accumulate the liability (**before close of the banking day**). Attach Schedule B to the Form 941 when filed.

Banking Days

- If your deposit is due on a non-banking day, make it by the close of the next banking day. Federal and state bank holidays, Saturdays and Sundays are non-banking days.

\$100,000 Deposit Rule, continued

For purposes of the \$100,000 rule, do not continue accumulating a tax liability after the end of a deposit period. For example, if a semiweekly schedule depositor has accumulated a liability of \$95,000 on a Tuesday (of a Saturday-through-Tuesday deposit period) and accumulated a \$10,000 liability on Wednesday, the \$100,000 next-day deposit rule does not apply. Thus, \$95,000 must be deposited by Friday and \$10,000 must be deposited by the following Wednesday.

However, once you accumulate at least \$100,000 in a deposit period, stop accumulating at the end of that day and begin to accumulate anew on the next day. For example, Fir Co. is a semiweekly schedule depositor. On Monday, Fir Co. accumulates taxes of \$110,000 and must deposit this amount on Tuesday, the next banking day. On Tuesday, Fir Co. accumulates additional taxes of \$30,000. Because the \$30,000 is not added to the previous \$110,000 and is less than \$100,000, Fir Co. must deposit the \$30,000 by Friday (following the semiweekly deposit schedule).

Example. Elm, Inc., started its business on April 1, 2008. On April 11, it paid wages for the first time and accumulated a tax liability of \$40,000. On Friday, April 18, 2008, Elm, Inc., paid wages and accumulated a liability of \$60,000, bringing its accumulated tax liability to \$100,000. Because this was the first year of its business, the tax liability for its lookback period is considered to be zero, and it would be a monthly schedule depositor based on the lookback rules. However, since Elm, Inc., accumulated a \$100,000 liability on April 18, it became a semiweekly schedule depositor on April 19. It will be a semiweekly schedule depositor for the remainder of 2008 and for 2009. Elm, Inc., is required to deposit the \$100,000 by Monday, April 21, the next banking day. **For further explanation of the look-back period see Publication 3151A page 5 or Publication 15 page 20.**

Summary of steps to avoid Failure to Deposit Penalties:

Make deposits on or before the deposit due date.

- Make your deposit any time between the payroll liability incurred date and the deposit due date.
- You are not required to wait until the due date nor will you receive a penalty for making deposits prior to the due date.
- Mail or deliver the Form 8109 deposit coupon with your payment so that it will arrive at the bank no later than the deposit due date.
- For deposits made by EFTPS to be on time, you must initiate the transaction **at least one business day before the date the deposit is due.**
- Accumulated tax liabilities of **\$100,000 or more on any day** during a deposit period, deposit the tax by the **NEXT banking day.**

Make deposits with an authorized financial institution (i.e. commercial bank) that is authorized to accept federal tax deposits.

Include a summary of your tax liability with Form 941.

- Monthly depositors use line 15 of Form 941.
- Semiweekly depositors use Schedule B, Employer's Record of Federal Tax Liability.

Additional information can be found in Publication 3151-A (Rev. 7-2007) Understanding Federal Tax Deposits or Publication 15 (Rev 2008).

How to Avoid an “Averaged” Failure-To-Deposit Penalty

IRS may assess an “averaged” failure-to deposit (FTD) penalty of 2% to 10% if you are a monthly schedule depositor and did not properly complete the monthly liability section (Part 2) of Form 941 when your total adjusted tax liability shown on Form 941 exceeded \$2,500.

IRS may also assess an “averaged” FTD penalty of 2% to 10% if you are a semiweekly schedule depositor and your total adjusted tax liability shown on Form 941 exceeded \$2,500 and you

- 1) completed the monthly liability section of Form 941 instead of Schedule B (Form 941),
- 2) failed to attach a properly completed Schedule B (Form 941), or
- 3) improperly completed Schedule B (Form 941) by, for example, entering tax deposits instead of tax liabilities in the numbered spaces.

The “averaged” FTD penalty is computed by taking your total adjusted tax liability shown on Form 941 and distributing it equally throughout the tax period. As a result, your deposits and payments may not be counted as timely because the actual dates of your tax liabilities cannot be accurately determined.

An “averaged” FTD penalty can be avoided by reviewing your return prior to filing it. Follow these steps before submitting your Form 941.

- If you are a monthly schedule depositor, report your tax liabilities (not your deposits) in the monthly liability section (Part 2) shown on Form 941. Verify that your total liability for the quarter on Part 2, number 15 equals your total adjusted tax liability shown on line 10 of Form 941.
- If you are a semiweekly schedule depositor, report your tax liabilities (not your deposits) on Schedule B (Form 941) in the lines that represent the dates your employees were paid. Verify that your total liability on the bottom of Schedule B (Form 941) equals your total adjusted tax liability shown on Line 10 of Form 941.
- Do not show negative amounts in the monthly liability section Schedule B (Form 941). If your prior period correction results in a decrease to your tax liability, reduce your liability for the day that you discovered the error by the tax decrease resulting from the error, but not below zero. Apply any remaining decrease to subsequent liabilities.

Schedule B (Form 941) Penalties

IRS uses Schedule B (Form 941) to determine if you have deposited your federal employment tax liabilities on time. If you do not properly complete and file your Schedule B (Form 941) with Form 941, IRS may propose an “averaged” failure-to-deposit penalty. See Deposit Penalties in section 11 of Pub. 15 (Circular E) for more information.

Who Must file Schedule B (Form 941)?

File Schedule B (Form 941) if you are:

- a semiweekly schedule depositor or
- a monthly schedule depositor who accumulated a tax liability of \$100,000 or more on any given day in the reporting period.

Completing the Schedule B Correctly

- On Schedule B (Form 941), list your **tax liability** for each payroll date.

Include:

- The federal income tax you withheld from your employees’ payroll and
- both employee and employer Medicare and social security taxes

Note. Subtract any advance earned income credit payments from your tax liability.

The most common errors and reason for Schedule B Penalties are:

- Failure to include a schedule B when required.
- Reporting the date and amount of the deposits on Schedule B rather than the amount of the tax liability on the date incurred.
- The total tax liability on Line 10 of the 941 does not match the total liability reported on Part 2 total on Line 15 or total liability on Schedule B.

Examples

The screenshot shows the 'Part 2: Tell us about your deposit schedule and tax liability for this quarter' section of Form 941. It includes fields for state abbreviation, deposit schedule, and monthly tax liability. A red box highlights the 'Total liability for quarter' on line 15, which is 11,300.00. Another red box highlights the 'Total taxes after adjustment for advance EIC' on line 10, which is 11,300.00. A red box also highlights the 'Total deposits for this quarter' on line 11, which is 12,000.00. A red arrow points from the line 10 box to the line 11 box, indicating a mismatch. The 'Total must equal line 10' note is also visible.

Line	Description	Amount
14	State abbreviation	AB
15	Total liability for quarter	11,300.00
8	Total taxes after adjustments	12,000.00
9	Advance earned income credit (EIC) payments	1,300.00
10	Total taxes after adjustment for advance EIC	11,300.00
11	Total deposits for this quarter	12,000.00
12	Balance due	700.00

Form 941 Semiweekly Depositor Liability Section Schedule B. Enter liability on the relevant pay dates.
 Note. The example below meets the \$100,000 dollar deposit rule. Therefore they are required to make all deposits on the next banking day.

Schedule B (Form 941):

Report of Tax Liability for Semiweekly Schedule Depositors
 (Rev. January 2005) Department of the Treasury — Internal Revenue Service

990306

OMB No. 1545-0029

Employer Identification number -
 Name (not your trade name)
 Calendar year (Also check quarter)

Report for this Quarter ... (Check one.)

- ☐ 1: January, February, March
☐ 2: April, May, June
☐ 3: July, August, September
☒ 4: October, November, December

Use this schedule to show your TAX LIABILITY for the quarter; DO NOT use it to show your deposits. You must fill out this form and attach it to Form 941 (or Form 941-SB) if you are a semiweekly schedule depositor or became one because your accumulated tax liability on any day was \$100,000 or more. Write your daily tax liability on the numbered space that corresponds to the date wages were paid. See Section 11 in Pub. 15 (Circular E), Employer's Tax Guide, for details.

Month 1

1		9		17		25	
2	145,054 . 88	10		18		26	
3		11		19		27	
4		12		20		28	
5		13		21		29	
6		14		22		30	185,887 . 43
7		15		23		31	
8		16	134,887 . 78	24			

Tax liability for Month 1: 445,640 . 10

Month 2

1		9		17		25	
2		10		18		26	
3		11		19		27	185,887 . 88
4		12		20		28	
5		13	175,854 . 43	21		29	
6		14		22		30	
7		15		23		31	
8		16		24			

Tax liability for Month 2: 342,842 . 41

Month 3

1		9		17		25	
2		10	187,878 . 87	18		26	
3		11		19		27	
4		12		20		28	
5		13		21		29	
6		14		22		30	
7		15		23		31	
8		16		24			188,887 . 80

Tax liability for Month 3: 354,888 . 77

Fill in your total liability for the quarter (Month 1 + Month 2 + Month 3) = Total tax liability for the quarter
 Total must equal line 10 on Form 941 (or line 5 on Form 941-SB).

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 119870

Total liability for the quarter
 1,142,749 . 28

Total Must - line 10 of 941!

Bottom
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 941

8 Total taxes after adjustments (Combine lines 6 and 7h) 1,142,749 . 28

9 Advance earned income credit (EIC) payments made to employees

10 Total taxes after adjustment for advance EIC (line 8 - line 9 = line 10) 1,142,749 . 28

11 Total deposits for this quarter, including overpayment applied from a prior quarter 1,186,749 . 70

12 Balance due (If line 10 is more than line 11, write the difference here.)

13 Overpayment (If line 11 is more than line 10, write the difference here.) 44,000 . 42

Check one ☒ Apply to next return. ☐ Send a refund.

You MUST fill out both pages of this form and SIGN it.

For Privacy Act and Paperwork Reduction Act Notice, see the back of the Payment Voucher. Cat. No. 170012 Form 941 (Rev. 1-2007)

How to Respond to Notices and Avoid Form 1099 Penalties

Some entities may receive Notice 972CG, which is a Notice of Proposed Civil Penalty. You will receive this notice and a listing of the information returns if you filed Forms 1099 or W-2G with missing or incorrect name/Taxpayer Identification Number (TIN) combinations. A name/TIN combination is incorrect when it does not match or cannot be found on the IRS files that contain Social Security Numbers and Employer Identification Numbers. Notice 972G proposes a penalty of \$50 for each return you did not file correctly. You should compare the listing with your records to determine:

- **If you took appropriate action to meet the requirements for reasonable cause, and**
- **If you must make an annual solicitation in the current year to avoid penalties in the future years.**

One way to obtain the necessary information and avoid penalties is to secure a Form W-9, Request for Taxpayer Identification Number and Certification, or an acceptable substitute. A W-9 is used by persons required to file information returns (such as Forms 1099-MISC, Forms 1099-R, or Forms W-2G) with the IRS to get the payee's correct TIN prior to making a payment to a vendor, especially a service provider vendor.

A Social Security Number (SSN) must be used with an individual name even though he or she may also have an Employer Identification Number (EIN). He or she must always furnish his or her individual name regardless of whether he or she uses a SSN or an EIN. A sole proprietor may also provide a business name or dba ("doing business as"), but the individual name must be listed first on the account with you.

Other businesses should enter the business name as shown on required federal tax documents. The dba may be listed on the second line "business name". The EIN of the entity should be entered in part I of Form **W-9** requesting the TIN.

Your TIN is not interchangeable with different names. A business Employer Identification Number (EIN) must be used for a partnership or corporation. A Limited Liability Company (LLC) may be a sole proprietorship, partnership, or corporation. A LLC that is a sole proprietorship must provide the social security number of the sole proprietor and not the EIN for the LLC.

The Form W-9 certifies for you that the payee's TIN is correct and the payee is a U.S. person. It also states the kind of business entity and may determine if you have a requirement to file an information report. The form is signed under penalty of perjury. Penalties may be applicable to payees for failure to furnish the TIN or providing false information. Payers may be subject to civil penalties for missing or incorrect information on the information reports.

U.S. resident aliens who are not eligible to receive a SSN must apply for an Individual Tax Identification Number (ITIN) on Form W-7, Application for IRS Individual Taxpayer identification Number. A Form W-9 is also used by individuals who have an ITIN.

Backup withholding will apply if:

- 1) The payee fails to furnish his or her SSN or TIN to you, or
- 2) The IRS notifies you to impose backup withholding because the payee furnished an incorrect TIN.

Tips for Obtaining “Good” TINs:

- Always obtain the contractor’s TIN before paying for services.
- Avoid abbreviating company names.
- If possible, refer to and use the same name as it appeared on the original application for the EIN (Form SS-4) or social security card.
- If you know a company has changed its name, ask if they have informed the IRS of the change. The IRS and SSA must be informed of any name changes.
- When filing Form 1099-MISC for a sole proprietor, always put the individual’s name, first, followed by the business name. For example, Joe’s Garage should be reported as Joseph Johnson, DBA Joe’s Garage. It does not matter whether you are using an EIN or SSN, the individual’s name must appear first.
- The best tool to help you gather good information on contractors and vendors is Form W-9 (or a substantially similar version). It is a good resource for obtaining correct payee names/TINs and other certifying exempt status for reporting purposes. In addition, the form specifically addresses the issue of sole proprietors. When properly completed, you will know if a contractor is a sole proprietor and therefore you will know to use the individual name first.

More information on backup withholding may be obtained in Publication 1281, Backup Withholding on Missing and Incorrect Name/TINs. For additional information refer to the instructions for the Form W-9. Please maintain the Forms W-9 in your files in event that the Internal Revenue Service requests verification of the name/TIN listed on the Form 1099.

If you have questions about withholding, information reporting, Forms 1099, or the CP2100 or CP2100A Notice(s) and listing(s), you may call your local ITG specialist or Martinsburg Computing Center (MCC) Information Reporting Program Customer Service Section Telephone: 866-455-7438 (toll free) . The telecommunication Device for the Deaf (TDD) number is (304)267-3367) (not a toll-free number). Hours: 8:30 a.m. to 4:30 p.m. Monday through Friday, eastern time, E-Mail: mccirp@irs.gov.

The table on the next page can be used as a quick reference should you receive a CP2100 or CP2100A notice.

What should you do if you receive a CP2100 or CP2100A notice?

What's the problem?	Compare the IRS listing to your records and...	Then...
Missing TINs	Begin or continue backup withholding immediately	<i>Solicit TIN from Payee...</i> <ol style="list-style-type: none"> 1. Initially (when payment was made) 2. First Annual Solicitation by December 31 of the year payment is made (for 2007 payment this was 12/31/07). 3. Second Annual Solicitation by December 31 of the following year (for 2008 payments this date is 12/31/08).
Incorrect TINs	<i>If they agree</i> (the TIN/name combination on the list match the W-9, W-2G, or other documents in your records)	<i>Send the 1st or 2nd "B" notice to the payee:</i> <ol style="list-style-type: none"> 1. You have 15 business days to send a "B" Notice to a payee, include a Form W-9. 2. Backup withhold from any reportable payments if the payee certification is not returned to you within 30 days after you receive the CP2100/2100A. 3. Do not backup withhold if the payee furnishes the required certification (Form W-9 in response to the 1st "B" notice, or Form SSA-7028 or IRS Letter 147C in response to the 2nd "B" Notice). 4. Keep these documents on file to show you have met the requirements for reasonable cause when the proposed missing or mismatch penalty notices are sent. 5. The 2nd "B" Notice should be sent to the payee if this is the second CP2100/2100A Notice you have received within three calendar years for this payee.
	<i>If they do not agree</i> , if could be because- <ol style="list-style-type: none"> 1. You put the incorrect information on the return; 2. The information changed after you filed it; or, 3. IRS misprinted the information in processing. 	<ol style="list-style-type: none"> 1. Correct & update your records. 2. Use the correct TIN/name information for future filing. 3. Make a note of the error in your records.

Following and documenting these procedures is a very important step to establishing "reasonable cause" when the Proposed Missing and Incorrect TIN Penalty notices are received.